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Report to the Chairman, Subcommittee on Oversight and Investigations, Committee on Energy and Commerce, House of Representatives

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ENERGY REGULATION

More Effort Needed to Recover Costs and Increase Hydropower User Charges

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Resources, Community, and
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The Honorable John D. Dingell
Chairman, Subcommittee on Oversight
and Investigations
Committee on Energy and Commerce
House of Representatives

Dear Mr. Chairman:

At your request, we evaluated the Federal Energy Regulatory Commission's (FERC's) responsibilities under section 10(e) of the Federal Power Act (FPA). Section 10(e) authorizes FERC to assess and collect six separate annual charges from licensees participating in FERC's hydropower licensing program. As agreed, with your office, however, we limited our examination of FERC's efforts to three annual charges—one related to recovering administrative costs and two to the use of federal lands for hydropower projects.

This report discusses FERC's efforts to (1) recover its own administrative costs and those costs incurred by other federal agencies in support of the program and (2) revise its regulations for computing charges assessed to licensees for their use of federal lands. As requested, the report also provides information on the potential costs to customers from changes in the way FERC established land use charges and the effect of land exchanges on FERC's assessment of land use charges.

In summary, we found that although more can be done, FERC has taken steps to increase its collection of administrative costs by including costs incurred by other federal agencies in its annual billings to licensees. FERC is also in the process of finalizing a rulemaking that revises the basis for valuing federal lands used for hydropower projects. An analysis of the potential impact of increased land use charges on licensees and/or their customers showed that the impact will likely be minimal. We also noted that land exchanges have not affected FERC's assessment process except where legislatively exempted.

FERC's Collection of Administrative Costs

Since the early 1920's, FERC and its predecessor agency (the Federal Power Commission) have collected their own administrative costs from hydropower licensees. However, until recently, FERC made no attempt to collect costs incurred by other federal agencies that provide assistance in administering the hydropower program. In late 1985 FERC contacted

eight assist federal agencies and gathered data on their expenditures (not otherwise reimbursed) in support of the hydropower program. As a result, FERC's May 1986 annual administrative charge billing of about $32.3 million (for fiscal year 1985 costs) included, for the first time, program-related costs incurred by three of these federal agencies amounting to about $2.8 million. One other assist agency provided data to FERC but could not quantify its dollar costs.

Four of the agencies did not provide administrative cost data to FERC primarily because they could not provide the required data according to FERC's reporting criteria (e.g. type of activity, type of hydropower application, and whether the cost was for a municipal or nonmunicipal project). In addition, two of these agencies, the Department of the Interior's Bureau of Land Management and the U. S. Department of Agriculture's Forest Service, reported that they were unsure of what portion of their hydropower-related administrative costs may be reimbursable under the Federal Land Policy and Management Act of 1976[1] (FLPMA), and what portion of their costs was reimbursable under the FPA. The Bureau of Land Management has subsequently devised a system by which administrative costs under the FPA can be identified and reported to FERC. The Forest Service, however, is still trying to develop a system that will identify FLPMA and FPA costs and an appropriate reporting methodology. Despite apparent difficulties, FERC plans to continue requesting administrative costs from assist agencies so they can be included in future annual billings. To encourage assist agencies' participation, FERC provided additional detailed guidance with its 1986 request letter to help the agencies in preparing their cost reports.

In a related matter, the Department of Energy's Inspector General (DOE/IG) in February 1986, reported that about $600,000 in interest costs could be saved if FERC shortened its annual billing cycle by 3 months. On the basis of an agreement reached on the recommendation during a December 13, 1985, closeout conference, FERC issued a proposed rulemaking on December 30, 1985, that incorporated the DOE/IG finding and requested comments on a requirement that licensees report their generation data on a fiscal rather than a calendar year basis. If the requirement is included in the final rule, the 3-month time lag that FERC is currently experiencing would be eliminated with a reduction in future interest costs.

[1]The Federal Land Policy and Management Act of 1976 established public land policy for administration, management, protection, development, and the enhancement of public lands, and other purposes.

FERC's Procedures for Assessing and Billing Federal Land Use Charges

FERC's current regulations for assessing federal land use charges were adopted in 1976. Since that time, the DOE IG has issued two reports (1981 and 1985) concerning the need to revise the 1976 regulations. Acknowledging that land values and interest rates—the two factors used in determining the charge—have changed since 1976, FERC issued a proposed rulemaking in December 1985 to revise its methodology for assessing land use charges. The former Chairman of FERC intended to place priority on revising the land use charges and issuing a final rule by October 1986.[2] This would represent an expedited effort since FERC's average time for issuing rulemakings has been about 18 months. In late September 1986, a FERC official told us that the October date would not be met because FERC currently plans to use land values proposed in a similar rulemaking being finalized by the Forest Service. The Forest Service expects to finalize its rulemaking by December 1986, and FERC expects to issue its final rule on land values shortly thereafter. If FERC's final rule is delayed too far into 1987, it may not be applied to land use charges until January 1, 1988, thus continuing the lower land use charges assessed by FERC for another year.

In a related matter, FERC is also considering a revision to its billings procedures for land use charges. This is in response to a February 1986 DOE IG report recommending that the Chairman, FERC, review the current policy of billing after each calendar year and consider pre-billing for these charges. The DOE IG concluded that FERC's current billing policy results in an annual interest cost to the federal government of $270,000. In response to the DOE IG recommendation, a policy paper on billing procedures has been requested for the Chairman's consideration and the topic placed on the Commission's calendar for December 1986.

FERC's land use responsibility also includes approving land exchanges and requests for exempting the exchange from further land use charges. A land exchange occurs when privately owned land outside a hydropower project's boundaries is exchanged for federally owned land within the project's boundaries. However, FERC's assessment of a federal land use charge has not been affected by land exchanges because the government still retains the exclusive right to use the land for water power purposes. Two land exchanges that did result in land use charges being exempted were congressionally approved.

[2]The Chairman, FERC, resigned his position in February 1986.

Impact of Increased Land Use Charges

While FERC's proposed rulemaking is expected to increase federal land use charges because of the increase in land values since 1976, there will be minimal economic affect on licensees or their customers. For example, FERC's assessment of increased land use charges on both large and small licensees indicated no significant impact on their ability to own or operate a project that uses federal lands. In the proposed rulemaking, however, FERC stated that if the final rule would have significant effect on a substantial number of small hydropower licensees, FERC will consider developing provisions in the final rule to mitigate any adverse impact that may occur.

We analyzed the potential impact of increased land use charges on customers of five selected large utilities by using localized agricultural land values and an 11-percent interest rate. Our analysis shows that even if land use charges to licensees increased 14-fold the maximum increase for residential customers would be about $0.35 annually.

Conclusions

FERC's current effort to provide additional guidance and clarification of cost data requirements appears to be a positive step in encouraging assist agencies to provide their administrative costs to FERC for billing licensees. However, FERC needs to continue its efforts to ensure that as much of FPA-related costs as possible are recovered. FERC's efforts to ensure the recovery of reasonable charges for use of federal lands and reduce interest costs from delayed billings to licensees also are in progress. Because of the potential for increasing federal revenue, we believe that action should be completed on the proposed rulemaking so that it will be effective on January 1, 1987.

Recommendations

We recommend that the Chairman, FERC, direct the Office of Program Management staff to work closely with Forest Service officials in the identification of administrative costs that may be reimbursable under FPA. We also recommend that the Chairman take steps to ensure that the ongoing rulemaking to revise land use charges and the annual billing procedures is completed in a manner that authorizes land use charges to become effective January 1, 1987.

Scope and Methodology

To evaluate FERC's assessment of annual charges, we reviewed applicable FERC legislation, regulations, orders, and records pertaining to the

hydropower licensing program. We also reviewed the DOE IG reports pertaining to the program, Department of Agriculture land value publications, and administrative cost information of other assist agencies that support the program. We interviewed officials of FERC, DOE IG, and other assist agencies. To assess the potential impact on licensees of increasing land use fees, we computed estimated electric power cost increases for customers of selected large hydropower licensees. (App. I contains a more detailed discussion of our objectives, scope, and methodology.)

We discussed our findings with FERC program and general counsel officials and have included their comments where appropriate. However, as agreed with your office, we did not obtain formal agency comments on this report.

As arranged with your office, unless you publicly announce its contents earlier, we plan no further distribution of this report until 30 days from its publication date. At that time, we will send copies to the Chairman, Federal Energy Regulatory Commission; the Director, Office of Management and Budget; and interested congressional committees. We will also make copies available to others upon request.

Sincerely yours,

J. Dexter Peach

J. Dexter Peach
Assistant Comptroller General

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Abbreviations

BLM	Bureau of Land Management
DOE/IG	Department of Energy's Inspector General
FERC	Federal Energy Regulatory Commission
FLPMA	Federal Land Policy and Management Act of 1976
FPA	Federal Power Act
FPC	Federal Power Commission
FS	U.S. Department of Agriculture's Forest Service
GAO	General Accounting Office
RCED	Resources, Community, and Economic Development Division

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Objectives, Scope, and Methodology

As requested in your October 3, 1984, letter, and in subsequent discussions with your office, we evaluated the Federal Energy Regulatory Commission's (FERC's) assessment of annual administrative and federal land use charges under section 10(e) of the Federal Power Act (FPA).[1] Although section 10(e) authorizes FERC to assess licensees up to six different annual charges, we limited our work to analyzing three charges related to administrative costs and federal land use fees. With regard to administrative charges, you specifically requested that we review FERC's criteria for other federal agencies' use when reporting their administrative charges in support of FERC's hydropower program. You also asked us to (1) evaluate the economic impact of higher land use charges on project licensees and their customers and (2) examine the impact of land exchanges (private land for federal land within a hydropower's project boundaries) on FERC's collection of federal land use charges.

To obtain information on administrative charges incurred by other federal agencies that support FERC's hydropower program, we contacted Washington, D.C., headquarters' officials in the Department of the Interior's U.S. Fish and Wildlife Service, Bureau of Land Management (BLM), and National Park Service; U.S. Department of Agriculture's Forest Service (FS); and Department of Commerce's National Marine Fisheries Service. For three other assist agencies, we relied on statements made by FERC officials or a review of correspondence from assist agencies to FERC. We also reviewed Department of Energy/Inspector General (DOE IG) reports regarding FERC's assessment of charges under the hydropower program.

To obtain information on FERC's criteria to assist agencies in reporting their administrative charges in support of FERC's hydropower program, we reviewed the criteria and discussed it with FERC officials and the assist agencies that we contacted.

To evaluate the economic impact of higher land use charges and the impact of land exchanges on FERC's collection of these charges, we interviewed officials of FERC, FS, and BLM. We reviewed FERC's regulations, proposed rulemaking and comments by respondents to the proposal, orders, records, and correspondence. To assess the potential impact of increased annual charges on licensees, we selected five large electric utilities and calculated the expected changes in customers' rates if land use charges were increased. We selected these licensees on the basis of

[1]Section 10(e) of the Federal Power Act is a 1935 reenactment without substantive change of section 10(e) of the Federal Water Power Act of 1920.

one or more of the following: the large percentage of hydropower projects they operate, project location to obtain geographic distribution of licensees, and availability of data to assess the potential rate changes. Comparable data from smaller unregulated licensees could not be obtained and verfied in the time allowed for the audit work. We did not include acreage for transmission line rights-of-way in our analysis of impact on consumers of electric energy because of the relative insignificance of this land use compared with the amount of land used for the hydropower project itself.

Our review was performed between June 1985 and April 1986. The views of directly responsible officials were sought during our work and are incorporated in the report where appropriate. However, as requested by your office, we did not obtain official agency comments on a draft of this report. Our work was performed in accordance with generally accepted government auditing standards.

FERC's Hydropower Charges

Background

The Federal Power Commission (FPC), predecessor to FERC, began licensing hydroelectric projects in 1920. According to the December 1985 notice of proposed rulemaking, FERC's hydropower program covered the licensing of approximately 858 nonfederal hydroelectric power projects. The locations or power capabilities of 283 projects were dependent on lands and waterways under federal jurisdiction. In carrying out its hydropower licensing activities, FERC is assisted to varying degrees by other federal agencies. Services rendered by these other agencies generally relate to prelicensing tasks.

Under Part I, section 10(e) of the FPA, FERC is required to assess annual administrative charges to hydropower project licensees as reimbursement for the costs incurred in administering the program. These costs include all operating costs for licensing and dam safety inspection activities. FERC is also required to assess annual land use charges to licensees for the use, occupancy, and enjoyment of federal land. In May 1986, FERC billed licensees over $34 million in fiscal year 1985 annual charges: $32.3 million for administrative costs of the program and $1.8 million for use of federal lands.

The FPA allows a partial or total exemption from payment of both administrative charges and federal land use charges for some licensees. States and municipalities, for example, are exempted from these charges if (1) the power generated is sold to the public without profit, (2) the power is used for state or municipal purposes, or (3) the project is primarily designed to provide for or improve navigation. Exemptions from annual administrative charges and federal land use charges vary from a fraction of 1 percent to a full 100 percent of the assessed charges. FERC's latest available data show that it exempted about $1.9 million in calendar year 1985. This included about $1.7 million in administrative charges for 32 partially or fully exempt municipal projects and $175,452 in federal land use charges for 20 partially or fully exempt projects. The $1.7 million is included in the FERC budget as an unreimbursable expenditure. The $175,452 represents income foregone because of the exemption clause of the act.

After FERC collects the annual charges, they are sent to the Treasury Department where they are distributed according to section 17(a) of the FPA. All administrative charges and penalty charges (which can be applied if the annual charge is not paid within 45 days of the billing date) are credited to the miscellaneous receipts account. Fifty percent of the federal land use charges is sent to the Reclamation Fund of the Department of the Interior, 37.5 percent is allocated to the states with

hydropower projects using federal lands, and the remaining 12.5 percent is retained by the Treasury in the miscellaneous receipts account.

DOE IG has issued two reports on FERC's assessment of charges under the hydropower licensing program.[1] The September 18, 1985, report concluded that (1) FERC was not recovering over $6 million in annual administrative costs incurred by FS and (2) FERC is undercharging hydropower licensees for use of federal lands by about $15.2 million annually because land values and interest rates are not current.[2]

The DOE IG report recommended that FERC recover administrative costs incurred by other federal agencies by identifying all federal agencies that incur significant costs under Part I of the FPA and requesting each agency to provide supportable evidence of costs incurred to FERC for use as a basis for billing hydropower licensees. With regard to federal land use charges, the DOE IG report recommended that FERC revise its regulations to base its land use charges on the current fair market value of land being used and the current long-term government borrowing rate.

In February 1986, the DOE IG issued a report on FERC's accounts receivable, billings, and collections of annual hydropower charges assessed under the FPA.[3] Regarding administrative charges and federal land use charges discussed in the report, DOE IG recommended that FERC shorten the billing cycle for administrative charges and review its current policy of billing land use charges after the end of each calendar year and consider developing a policy requiring advance billing of the land use charges.

Administrative Charges

The administrative costs FERC incurs in conducting its licensing and dam inspection activities are almost totally offset by annual charges billed to licensees. In 1985 FERC billed licensees $26.3 million for administrative

[1]Report on Assessment of Charges Under the Hydropower Licensing Program (DOE/IG-0178, Dec. 22, 1981) and Report on Assessment of Charges Under the Hydropower Licensing Program (DOE/IG-0219, Sept. 18, 1985).

[2]As discussed later on page 13, FS officials told us that the $6 million was total administrative costs related to hydropower program activities, but FS officials were unsure of what part of their costs should be reported to FERC for collection under FPA.

[3]Report on Accounts Receivable, Billings and Collections of the Federal Energy Regulatory Commission (DOE IG-0224, Feb. 18, 1986).

costs incurred in fiscal year 1984. These charges ranged from a minimum of $5 to over $1 million per project. In May 1986, FERC billed annual administrative charges of $32.3 million for fiscal year 1985.

FERC allocates its administrative costs among hydropower project licensees on the basis of (1) fixed charges written in the licenses, (2) rated horsepower for licensees with small projects—2,000 horsepower or less, and (3) rated horsepower plus annual energy generation for major licensees with projects over 2,000 horsepower. After the total costs are adjusted for fixed and small project charges, the remainder is prorated among municipal and nonmunicipal licensees. Once the cost allocation is made, municipal licensees charges are reviewed for possible exemptions and the amounts billed are reduced accordingly.

Prior to fiscal year 1985, FERC's practice was to bill hydropower licensees only for FERC costs. As stated earlier, however, other federal agencies provide assistance to FERC and, as a result, also incur administrative costs related to FERC's hydropower program. Other agencies' assistance to FERC primarily consists of commenting on (1) ways to avoid or minimize potentially adverse impacts of specific hydropower project proposals, (2) means to ensure that use of the public lands for hydroelectric purposes will not substantially detract from or conflict with the other purposes for which the public lands are managed, and (3) environmental impact statements, where required.

In August 1985, FERC initiated action to address the DOE/IG recommendation to recover administrative costs incurred by other agencies. Between August 30, 1985, and October 25, 1985, FERC identified and sent letters to eight federal agencies that may have incurred costs in support of FERC's hydropower program and requested that the agencies provide FERC with their fiscal year 1985 costs by November 15, 1985.[4] FERC planned to include these costs in its annual billings. FERC requested that the agencies' costs be reported by (1) specific activity or work performed, listing the organizational unit involved and the purpose of the activity, (2) type of hydropower application involved (e.g., preliminary permit, exemption, and license), and (3) municipal and nonmunicipal category.

[4]Department of Interior's Bureau of Indian Affairs, Bureau of Land Management, Bureau of Reclamation, Fish and Wildlife Service, and National Park Service; U.S. Department of Agriculture's Forest Service; Department of Commerce's National Marine Fisheries Service; and Department of Defense's Army Corps of Engineers.

Four agencies submitted data, (National Park Service, Fish and Wildlife Service, U.S. Army Corps of Engineers, and National Marine Fisheries Service) but FERC was only able to use data from three agencies. FERC's Chief of Program and Fees Branch said that the data submitted by the National Park Service was not used because it did not meet FERC's criteria for supportable administrative costs.[5] Consequently, FERC's May 1986 billing for fiscal year 1985 costs included only about $2.8 million for three of the four agencies that identified costs attributable to Part I of the FPA. These additional administrative costs consisted of $1.5 million for the Fish and Wildlife Service, $732,000 for the U.S. Army Corps of Engineers, and $489,000 for the National Marine Fisheries Service.

The remaining four agencies (Bureau of Indian Affairs, Bureau of Reclamation, Bureau of Land Management, and U.S. Department of Agriculture's Forest Service) indicated that they would not be submitting fiscal year 1985 cost data to FERC. According to the Chief of FERC's Program Review and Fees Branch, the Bureau of Indian Affairs verbally informed FERC that they would not be submitting any cost data. The Bureau of Reclamation notified FERC that the requested data could not be provided for fiscal year 1985, but it will attempt to provide it for fiscal year 1986. Both FS and BLM submitted responses stating that the requested data could not be provided under their current time management systems.

Officials of both FS and BLM further reported that they were uncertain what portion of their administrative costs is related to FERC's hydropower program and what portion is related to their responsibilities under the Federal Land Policy and Management Act of 1976 (FLPMA), which also contains a reimbursement provision. Under section 501 (a)(4) of FLPMA, the holder of an FPA license must also secure a FLPMA right-of-way grant from either FS or BLM to authorize the use of public land under the license. According to the Director of BLM, the rationale for this dual authorization requirement is to ensure that the use of the public lands for hydropower purposes will not substantially detract from or conflict with the other purposes for which the public lands are managed under FLPMA. Under section 504 (g) of FLPMA, both agencies are authorized to obtain reimbursement for all reasonable administrative costs incurred in processing right-of-way applications for hydropower projects. Both agencies can also obtain reimbursement for costs incurred in inspecting

[5]Although the National Park Service identified 37 work months in support of FERC's program, it was uncertain how to cost out the time expended. According to a National Park Service official, the requested costs could not be broken down by FERC's reporting criteria.

and monitoring construction, operation, and termination of a hydropower project—the same kinds of effort expended for FERC hydropower applicants.

FS has not been charging a fee for the special-use authorizations that it issues for hydropower projects that require rights-of-way on National Forest System lands. However, in its response to FERC, FS stated that although it has not yet published regulations implementing reimbursement of administrative costs under FLPMA, it plans to publish a proposed rulemaking in 1986. FS officials explained that until these proposed regulations are further along, they are unsure what part of FS costs should be reported to FERC for collection under the FPA and what part should be considered for reimbursement under the FLPMA. FS informed FERC that the earliest date that it could report the data would be fiscal year 1988 because FS still has to publish its administrative cost-recovery regulations, identify costs that are recoverable under the FPA, and work out an appropriate method to identify and report the data to FERC. Until such time as actions are completed, any administrative costs incurred to support the hydropower program will go unreimbursed.

In contrast to FS, the Chief of BLM's Division of Rights-of-way told us that BLM is currently being reimbursed under FLPMA for administrative and other costs incurred in granting rights-of-way and temporary use permits on BLM land. To comply with FERC's request for cost data, he told us that subsequent to its initial response, BLM has devised a system by which administrative costs incurred for work done under FPA can be identified and reported to FERC. BLM began implementing this system on October 1, 1986.

Assist agencies officials that we contacted after FERC's request letters had gone out told us that they believe the criteria for reporting administrative cost data to FERC were feasible and workable. However, most of the officials were unprepared to accumulate and report the requested data because FERC did not give enough advance notice. They said that, in subsequent years, it would be easier if they know the request for data would be a continuing requirement. Several officials, however, doubted that it would be cost-effective for their agencies to develop an accounting system modification to capture the cost data as requested by FERC. Accordingly, in some instances, the cost data submitted would have to be a reasonable estimate.

Although the agencies officials believed that the criteria were feasible and workable, some were unclear as to what was required to satisfy the

data request. Even after obtaining clarification from FERC, the officials said that it was difficult for them to determine (1) how FERC distinguished between municipal versus nonmunicipal projects and, therefore, what assist work had been done for each type of project, (2) what part of the work was properly chargeable to FERC assistance as opposed to their own respective area of responsibility, (3) what proper "overhead" rates were applicable, and (4) how to cost-out identified staff time. Officials believed that future data request submissions should be clarified regarding these four factors.

FERC sent follow-up letters to the eight assist agencies in March 1986 emphasizing the recurring need to obtain annual administrative cost data. FERC informed the agencies that it would be requesting fiscal year 1986 cost data in September 1986 and asked them to begin taking measures to identify those costs. According to the Chief of FERC's Program Review and Fees Branch, FERC had no plans at that time to provide any additional guidance to the assist agencies for developing the requested cost data.

During our evaluation, we discussed with responsible FERC officials the concerns expressed to us by assist agency officials and their reluctance to spend a lot of time attempting to respond to FERC's request until additional guidance and clarification of the criteria were made available. As a result, the Chief of the Program Review and Fees Branch told us that she was proposing that FERC send additional guidance to the assist agencies with the data request letters. She also planned to include the name of a contact person in its budget office as a source of further clarification on data collection and presentation if needed. On September 26, 1986, FERC sent out the request letters including the additional guidance and clarification. Agencies were asked to respond by November 15, 1986. No responses had been received at the time our report was issued, so we could not assess the effectiveness of the guidance.

Federal Land Use Charges

In 1942, FERC began computing its land use charges by multiplying a national average value per acre of land used times a fixed 4-percent interest rate to obtain a uniform annual per-acre charge. In 1962, FERC established a national average land value of $60 per acre and retained the 4-percent interest rate. This resulted in an annual charge of $2.40 per acre for all federal lands used by the licensees of hydropower projects. FERC's current regulations for assessing federal land use charges were issued in FPC Order No. 560, dated December 29, 1976. The order revised both the land value index and the interest rate that are

used to compute federal land use charges. The land value index was increased from $60 to $150 per acre (the increase to be applied on an incremental basis over 3 years beginning in fiscal year 1977). FERC also increased the land value for transmission line rights-of-way usage of federal lands from $16.50 to $75 per acre—one-half of the land value index.

In an effort to ensure that the rate of return would remain current, FPC's Order No. 560 also increased the interest rate from a fixed rate of 4 percent to a fluctuating interest rate starting at 6-3/8 percent for fiscal year 1977. Although the FPA does not require the use of any particular interest rate, FPC selected the rate used by the United States Water Resources Council for water resources planning as being an appropriate rate for computing hydropower land use charges and incorporated the interest rate into Order No. 560. The rate was based primarily on the average yield of long-term (15 years or more to maturity) U.S. interest-bearing securities. The fluctuating interest rate can be adjusted each year to reflect changes in yield and the associated changing federal borrowing costs, but because of a statutory requirement (pursuant to Public Law 93-251), the Water Resources Council could not change the rate by more than one-quarter of a percent in any year. (FPC's acceptance of the rate in Order No. 560 also precludes any changes without a further rulemaking). The federal government's long-term borrowing rate, however, has recently been significantly higher than the rate FERC uses. For example, the interest rate FERC used had increased to 8-3/8 percent by fiscal year 1985, while the Treasury's long-term borrowing rate for bonds was 10.79 percent for that year. In September 1986, this interest rate was about 7.5 percent.

In fiscal year 1985, FERC billed licensees about $1.8 million for use of federal lands, including transmission line rights-of-way. This amounted to $12.56 per acre for federal lands used by hydropower projects and $6.28 per acre for the project's transmission line rights-of-way.[6] These annual charges ranged from $3 to $176,600 per project. In 1985, the 283 hydropower projects used about 173,000 acres of federal lands in 25 states and Puerto Rico. Most of the federal lands are located in western states; California and Washington account for about 72,900 acres, or about 42 percent, of the total federal lands used by hydropower projects. According to FERC's Notice of Proposed Rulemaking, the 283 projects are held by approximately 148 licensees.

[6]These annual charges were computed by multiplying $150 per acre for hydropower projects and $75 per acre for transmission line rights-of-way times the interest rate of 8-3/8 percent.

FERC Proposes to Increase Land Use Charges

As a result of the two DOE IG reports on assessing hydropower charges (discussed earlier), the former Chairman of FERC notified the Chairman, Subcommittee on Oversight and Investigations, House Committee on Energy and Commerce, on October 25, 1985, that FERC was planning to take action on DOE IG recommendations. FERC's former Chairman said that FERC would prepare a proposed rulemaking to modify its land use charge regulations to reflect revised land values and interest costs. The FERC letter also responded to the Subcommittee Chairman's earlier concern about the length of time for FERC to complete the rulemaking, namely that FERC officials had stated that the rulemaking process takes about 18 months. The former Chairman's letter informed the Subcommittee that this rulemaking would receive priority and FERC would attempt to complete it in 12 months and issue the final rule by October 1986.

On December 30, 1985, FERC issued a notice of proposed rulemaking on revising the methodology for assessing federal land use charges and requested comments from interested parties.[7] FERC's proposed rulemaking identified several alternatives for computing land use charges, including its traditional method of multiplying a per-acre land value index by a rate of return.

The proposed rulemaking identified two alternative land value indexes—one based on agricultural real estate values and another based on linear rights-of-way (value of federal land used by projects such as reservoirs, canals, ditches, pipelines, and transmission lines, which are required to obtain federal rights-of-way to cross federal lands)—that could be used in its traditional method of computing land use charges.

FERC proposed a land value index based on the Department of Agriculture's value per acre for farm land on a state-by-state basis. FERC noted, however, that these land values typically include the value of land and buildings. Since federal land used in hydropower projects typically does not include buildings, FERC would have to compute the average value per acre of land without buildings. Commenters were requested to discuss how this index could be adjusted to eliminate the differential between farm real estate values and the values of the land used for hydropower projects.

[7]Notice of Proposed Rulemaking on Revisions to the Billing Procedures for Annual Charges for Administering Part I of the Federal Power Act and the Methodology for Assessing Federal Land Use Charges, 51 Fed. Reg. 211 (1986).

FERC also proposed use of a land value index based upon work being done by FS and BLM in valuing linear rights-of-way. FS and BLM are jointly conducting a market survey to establish representative market values for various types of linear rights-of-way crossing land administered by the two agencies. The market survey data will be used to establish geographic zones of similar land values from which to develop a rental schedule for linear rights-of-way. Zones of similar value will be developed on a state or smaller subdivision basis. The per acre charges resulting from this survey are expected to be calculated according to a formula that includes the land value and a rate of return.

In the proposed rulemaking, FERC stated that FS and BLM were expected to periodically revise their land rental schedules to reflect changes in land value or rate of return. FERC said that one of its options would be to use the same per-acre charge (land value and interest rate) used by FS and BLM or use the land values upon which the FS/BLM charges are based in combination with FERC's own rate of return. Under either alternative, a licensee would submit data to FERC indicating how many acres of federal land used by its hydropower project lie within each zone. FERC said this method may be more representative of the value of land used for hydropower projects than a valuation of farm lands or any other information currently published.

FERC also proposed to eliminate the 50-percent discount for transmission line rights-of-way and charge the same per-acre value it does for hydropower projects using federal lands.

In determining the rate of return that would be applied to the above land values, FERC proposed to continue using the long-term United States marketable securities interest rate as a reasonable means by which to determine the rate of return for using the government's land. However, FERC proposed to eliminate the 0.25 of a percent per-year limitation on adjustments to the interest rate.

Although FERC proposed to continue computing land use charges by the traditional method (multiplying a per-acre land value by a rate of return), it recognized that other methods of valuing federal land used do not require computation of per-acre-values. FERC's proposed rulemaking, therefore, requested comments on other methods of valuing federal land use such as a percentage of gross income or a flat rate per kilowatt-hour of electricity produced by the hydropower project. FERC requested comments on whether (1) a charge that is predicated on the amount of generation or sales from a project can reasonably be related to the portion

of the project that occupies federal land, (2) retention or abandonment of the existing formula would better avoid unreasonable increases in the price of power paid by consumers, (3) licensees should be allowed to submit independent appraisals to contest the accuracy of an annual land use charge, and (4) an appraisal system could be the sole basis for determining fair market value of federal land use. Commenters were requested to identify the standards and criteria that should be used to make appraisals.

Comments on FERC's Proposed Rulemaking

By the March 4, 1986, deadline for comments on the proposed rulemaking, FERC had received 15 comments, primarily from licensees and a trade association group. Not every commenter addressed every issue in the proposed rulemaking. A general overview of the comments is given below.

Our review of the comments shows that six commenters who addressed the issue were in favor of retaining FERC's existing formula for computing federal land use charges. All commenters were opposed, however, to both of FERC's proposals for indexing land values. Ten of the commenters stated that the agricultural real estate values index did not accurately reflect the value of federal lands used by hydropower projects, and all of the commenters stated that FERC presented insufficient information upon which to judge the merits of the linear rights-of-way index. The commenters generally stated that if FERC decided to use the agricultural real estate value index, then it should continue to use the national average land value, rather than change to a state-by-state average land value for calculating annual charges. The commenters explained that if FERC chose this option, it should not use the current national average land value of agricultural lands (about $591 per acre in 1985), but rather FERC should index its current national average land value ($150 per acre) to reflect the percentage change that has occurred in land values since FERC last revised its land use charge regulations. For instance, if agricultural land values have gone up 50 percent since 1976, the new land value would be $225 per acre ($150 plus 50 percent times $150), rather than $591 per acre.

Ten commenters supported FERC's proposal to continue its present method of using the interest rate of long-term marketable securities to determine the rate of return for valuing federal lands. They were opposed, however, to FERC's proposal to abandon the annual limitations

on adjustments to the interest rate and stated that some type of limitations on annual interest rate adjustments was still needed. Some commenters said this limitation is being consistent with the provision in the FPA to guard against price increases to consumers due to annual land use charges.

Finally, eight commenters were opposed to FERC's proposal to eliminate the discount for transmission line rights-of-way usage of federal lands. Several commenters referred to FERC's 1976 order that established the discount because of the potential for multiple uses of the land. One commenter pointed out the public benefit of having access to otherwise inaccessible areas because of cleared rights-of-way.

A FERC attorney responsible for coordinating the proposed rulemaking told us that a firm schedule has not been established for completing the analysis of the rulemaking comments and submitting a final proposed rule to FERC Commissioners for approval. According to this attorney, FERC is working very closely with FS officials and is considering adopting the FS fee policy proposal (linear rights-of-way) for assessing annual land use charges. By letter dated July 7, 1986, FS asked FERC to coordinate the development of its fee program with that of FS and BLM so that they can be as consistent as possible. FERC responded by letter on August 8, 1986, stating that the linear rights-of-way evaluation may be more representative of the type of land used in hydropower projects than are farm lands or other real estate. FERC stated that the FS/BLM land valuations data may be very relevant and helpful in deciding what method and data to use in its final rule. The FS issued its proposed policy on linear rights-of-way on August 14, 1986. According to the Chief of FERC's Program Review and Fees Branch, FERC has decided to wait for completion of the FS rulemaking, which is expected to be completed by December 1986. Consequently, FERC's October 1986 deadline for issuing its final rule will have to be extended. The FERC attorney also told us that some slippage can be tolerated because a final rule can be issued after January 1, 1987, and FERC can make it retroactive to that date.

Impact of Increased Land Use Charges on Customers

The potential effect of higher land use charges on licensees has been examined from two perspectives—the impact on customers and the impact on the licensees. We assessed the impact of higher land use charges on the utilities' customers, rather than on the licensee, on the basis of the assumption that state public utility commissions generally allow electric utilities to pass through to their customers increased operating costs over which the utility has no control.

In five utilities that we selected to test, we found that increasing federal land use charges would likely result in only small increases in electric utility costs. This cost increase does not appear to have any significant adverse economic impact on the various customer classes (residential, commercial, and industrial) of the five utilities included in our review. The utilities are located in four states (California, Georgia, Oregon, and Washington) that account for about 47 percent of the hydropower projects that are assessed a land use charge by FERC. Four of the five utilities were selected because each had the highest land use charge in their state. In addition, we selected a second utility in California because its average farm land values were higher than those in the other three states. Therefore, an increase in federal land use charges based on state-by-state farm land values would be expected to have a greater economic impact on California customers than on customers of utilities in the other three states included in our review.

Our analysis compared customers' average 1984 annual electric costs with increased costs that could result from higher FERC land use charges. In computing the potential impact, we used FERC's current national land value of $150 per acre as our base and increased it to the respective farm land value in each of the four states included in our review. According to the agricultural land value index, these values ranged from $481 per acre in Oregon to $1,577 per acre in California. We used two interest rate assumptions in computing the potential impact. The 8-1/8 percent interest rate was used by FERC to compute fiscal year 1984 land use charges. The 11-percent interest rate approximates the average yield on 30-year government securities projected by Data Resources, Inc., under a high energy-price scenario and was used to estimate the impact that a substantial increase in interest rates (about 35 percent) would have on land use charges.[8]

Table II.1 shows the potential impact of increased federal land use charges on customers of electric utilities included in our review.

[8]Data Resources, Inc., Long-term Review—The Pessimistic Projections, spring 1986.

Table II.1: Impact of Increased Land Use Charges on Consumers of Energy for 1985

	Company				
	A	B	C	D	E
Acres[a,b]	1,419	13,837	17,025	5,227	3,840
Fiscal year 1984 annual charge ($150 x acres x 8-1/8%)[b]	$17,292	168,877	213,038	63,703	46,802
1985 state average land value per acre[c]	$735	1,577	1,577	481	775
Estimated annual charge (state average land value x acres x 11%)[d]	$114,726	2,400,388	2,953,327	276,561	327,360
Impact on residential customers					
Average kWh sold per customer[e]	9,855 9,855	6,147 6,147	6,557 6,557	12,644 12,644	14,259 14,259
Costs per kWh sold (cents)[f]	6.5302 6.5305	7.5390 7.5429	6.7541 6.7589	4.4732 4.4752	4.7300 4.7324
Annual costs per customer[f]	$643.55[g] 643.58[h]	463.42[g] 463.66[h]	442.87[g] 443.18[h]	565.59[g] 565.84[h]	674.44[g] 674.79[h]
Increase in annual costs	- $0.03	- 0.24	- 0.31	- 0.25	- 0.35
Impact on commercial customers					
Average kWh sold per customer[e]	74,938 74,938	53,957 53,957	49,187 49,187	69,790 69,790	68,770 68,770
Costs per kWh sold (cents)[f]	6.7788 6.7791	8.5439 8.5484	7.6143 7.6195	5.4138 5.4162	4.4750 4.4774
Annual costs per customer[f]	$5,079.90[g] 5,080.12[h]	4,610.03[g] 4,612.60[h]	3,745.25[g] 3,747.80[h]	3,778.29[g] 3,779.97[h]	3,077.46[g] 3,079.11[h]
Increase in annual costs	- $0.22	- 2.57	- 2.55	- 1.68	- 1.65
Impact on industrial customers					
Average kWh sold per customer[e]	1,548,012 1,548,012	7,475,662 7,475,662	14,574,058 14,574,058	16,334,519 16,334,519	1,270,542 1,270,542
Costs per kWh sold (cents)[f]	4.5515 4.5518	7.1093 7.1131	6.8673 6.8720	4.5600 4.5620	2.7537 2.7551
Annual costs per customer[f]	$70,457.77[g] 70,462.41[h]	531,467.24[g] 531,751.31[h]	1,000,844.28[g] 1,001,529.27[h]	744,854.06[g] 745,180.76[h]	34,986.92[g] 35,004.70[h]
Increase in annual costs	- $4.64	- 284.07	- 684.99	- 326.70	- 17.78

[a]Because of rounding of acres to whole numbers, calculations of annual charges are slightly different from actual fees charged by FERC.

[b]FERC's Records.

[c]USDA Agricultural Land Values and Market Outlook and Situation Report, August 1985. Values for buildings were deleted from land values shown in this report.

[d]Data Resource, Inc., Long-term Review—The Pessimistic Projection, spring 1986.

[e]FERC's Form No. 1 Annual Report of Electric Utilities, Licensees, and Other (Class A and Class B).

[f]Annual costs per customer is calculated by multiplying average kWh sold per customer by costs per kWh sold.

[g]Based on FERC's fiscal year 1984 annual charge at $150 per acre with an 8-1/8-percent interest rate.

[h]Based on state average land value per acre with a 11-percent interest rate.

As shown in table II.1, increased annual electric costs to various customer classes of selected utilities are small even if land values and interest rates increased significantly above the current levels. Our analysis shows that increased annual costs ranged from $0.03 to $0.35 for residential customers (annual costs ranging from about $443 to $675), from $0.22 to $2.57 for commercial customers (annual costs ranging from about $3,079 to $5,080), and from $4.46 to $684.99 for industrial customers (annual costs ranging from about $35,005 to $1,091,529).

FERC's assessment of the potential impact of the rulemaking was oriented toward the licensee. With respect to large projects, FERC noted that significant capital resources are required to plan, construct, and operate a large project. Because annual fees for the use of federal land currently constitute a small portion of these costs, FERC believes that it is unlikely that there will be a significant impact on these licensees no matter which method is ultimately chosen to calculate these annual charges.

FERC does not expect that small project licensees will be required to make large payments as a result of increased land use charges. In the proposed rulemaking, FERC stated that it had studied 72 of the 283 projects using federal lands and noted that a relationship exists between the size of the project and the amount of the federal land used. For example, the 24 small projects (1.5 megawatts or less) included in FERC's study generally had a smaller number of acres (average of 23 acres) in the project than did the larger projects.

FERC's proposed rulemaking also stated that even if the cost increase is large, in relation to the entire cost of the project, it is unlikely that annual charges would have a material effect upon the ability of any small project licensee to own or operate a project that uses federal land. FERC explained that the reason for this is that none of the methods being considered in its proposed rulemaking would assess a substantial charge for the use of 23 acres (the average size of small projects in FERC's study). FERC stated, however, that if it appears that the final rule will have a significant effect on a substantial number of small projects, it will consider including provisions in the final rule to mitigate any adverse impact on small licensees. FERC received only one comment that specifically addressed the potential impact of increased land use charges on customers. The commenter stated that certain FERC land use charge proposals could increase the utility's customer costs by more than $10 per year.

Exemptions From Land Use Charges Due to Land Exchanges

According to the Director, FERC's Division of Project Management, a land exchange occurs when privately owned land outside the project boundaries is exchanged for federally owned land within the project boundaries. Although FERC's assessment of federal land use charges is generally not affected by land exchanges, two cases have involved land exchanges where legislation was passed to exempt the hydropower project licensees from further land use charges.

Under section 24 of the FPA, when an application for a hydropower license is filed with FERC, the federal lands are withdrawn and reserved as water power sites (power withdrawal) until otherwise directed by FERC or the Congress. If a land exchange for hydropower purposes occurs, FERC's general policy is to deny requests for the release of the power withdrawals because the federal government still retains the exclusive right to use the land for water power purposes. Since the land is subject to a continuing power reservation and the federal government continues to hold the full title for water power purposes, FERC continues to assess annual land use charges because the licensee is obligated to reimburse the federal government for the use of the land when engaging in water power projects.

FERC's denial of a request for the release of a power withdrawal and fee waiver can be overruled by congressional action. FERC officials told us of two specific instances when this was done. On October 19, 1984, the Congress directed FERC (Public Law 98-496) to waive the charge required to be paid under section 10(e) of the FPA for the use of any interest of the United States in land lying within the boundaries of the South Carolina Public Service Authorities Santee-Cooper hydroelectric project. This action was taken after FERC had denied a request for a reduction or waiver of annual charges for a contemplated land exchange by the South Carolina Public Service Authority for FS-managed land in the Francis Marion National Forest.

On October 30, 1984, the Congress approved the exchange of government-owned land in the Sabine National Forest to the Sabine River Authority of Texas (Public Law 98-571). Section 4(a) of the act directed FERC to waive the charges required to be paid under section 10(e) of the FPA for the use of the land. Although the Sabine River project had been exempted by FERC from paying the annual charges during the period 1970 through 1983, the licensee was required to file for the exemption each year. The congressional action in Public Law 98-571 removed the annual requirement.

FERC's Response to DOE/IG Recommendations for Changes in Billing Procedures

In its February 18, 1986, report on FERC's billings and collections of annual hydropower charges, DOE/IG recommended that FERC (1) consider billing its licensees in advance for land use charges rather than after the year has passed as it is currently doing and (2) expedite its billing procedures for administrative charges. FERC is currently taking action to comply with the DOE/IG recommendations.

The DOE/IG recommended that the Chairman review FERC's current policy of billing after the calendar year and consider advance billing for land use charges. The DOE/IG found that rather than collecting charges in advance as other federal agencies are doing, FERC bills hydropower licensees for land use charges after the end of the calendar year (June of the following year). The DOE/IG concluded that FERC's billing policy results in an 18-month delay (June of the following year rather than January of the current calendar year) and an annual interest cost to the federal government of $270,000 ($1.8 million in land use charges times a 10-percent interest rate times an 18-month time period). The report also noted that although FPA is silent as to when the charges should be billed, other federal agencies with land leases are billing in advance as required under FLPMA.

In response to the recommendation, a policy paper on billing procedures has been requested for the Chairman's consideration, and time has been reserved on the Commission's calendar for December 1986 to discuss this issue.

FERC currently accumulates its administrative costs on a fiscal-year basis, while licensees submit their annual energy generation data by February 1, for the preceding calendar year. FERC uses the generation data in allocating its administrative costs. Because licensees are allowed to report on a calendar-year basis, FERC's billing date is delayed by as much as 3 months. The DOE/IG concluded that the delay in collecting generation data and billing licensees resulted in an increased interest cost to the federal government of about $600,000 for the 3-month lag from November 1 to February 1. The DOE/IG recommended that FERC require its licensees to submit their generation data on the same fiscal-year basis that FERC uses, thus eliminating the 3-month time lag.

On December 30, 1985, FERC issued a proposed rulemaking that would require licensees to submit their generation data on a fiscal-year basis and file the reports 3 months earlier (by November 1 for the preceding fiscal year, rather than February 1 of the next year). FERC's proposed rulemaking stated that this would eliminate the loss of interest to the

U.S. Treasury, which results from the 3-month lag between the time FERC's reimbursable costs are incurred and the time the licensees file their generation data. FERC noted that depending on when the rule was to become effective, for that year only, the effect of the rule might be that licensees would report generation data for the months of October, November, and December twice; first, when they make the February 1 filing under the old rule and then again, when they make their November 1 filing under the new rule. FERC explained, however, that since the reimbursable costs have always been based on the fiscal year, this requirement should not result in an increase in the amount of annual charges paid.

Our review of comments received by FERC in March 1986 on the proposed rulemaking shows that most commenters generally supported FERC's proposed revisions to its billing procedure for hydropower administrative charges. Several commenters suggested, however, that FERC's billing procedures be revised in a manner that did not result in double billing for the transition months of October, November, and December.

Conclusions

FERC has recently initiated actions to improve its performance in assessing and collecting administrative and land use charges from its hydropower licensees. This has been done by asking assist agencies to provide their incurred administrative costs to FERC and by issuing a proposed rulemaking on land use charges and licensee reporting requirements. The partial success of its initial efforts to increase its administrative cost collections and the potential for (1) obtaining a more reasonable fee for federal land use and (2) reducing the interest costs to the federal government makes it imperative that FERC give priority attention to quickly completing the actions already underway.

FERC's initial effort to obtain the administrative costs incurred by other federal agencies resulted in increasing FERC's billings to licensees for fiscal year 1985 costs by about $2.8 million. It also established a framework for continuing to collect these administrative costs that had previously gone uncollected. However, four of the eight agencies that FERC contacted did not respond with the requested fiscal year 1985 cost data and one agency responded but the data were unusable. Some agency officials expressed concern that, although FERC's criteria for determining and reporting the cost data were reasonable, additional guidance and clarification were needed in formulating their response. FERC responded to those concerns by including further guidance and clarification in a September 26, 1986, letter to assist agencies requesting cost data for

fiscal year 1986. Two of the agencies—BLM and FS—officials said that they were unable to determine whether their administrative costs were reimbursable under FLPMA or FPA. BLM is already collecting some incurred administrative costs under FLPMA and indicated that on October 1, 1986, it would begin collecting FPA-related cost data. FS is not yet collecting any costs, and officials reported to FERC that it would be fiscal year 1988 before FS could respond to the data request. We believe that FERC should work closely with the FS to ensure maximum recovery of all applicable incurred administrative costs.

FERC's prior lack of action in updating the value of federal lands used by hydropower licensees and assigning an appropriate interest rate for computing land use charges is also being corrected. Its December 30, 1985, proposed rulemaking addresses both the land value and interest rate issues. FERC's final rulemaking will likely result in increase land use charges as compared with previous levels, thus providing a greater return to the government for the land used. It does not appear, however, that land use charges will adversely affect hydropower licensees' operations. Our analyses of how large increases in land use values and interest rates would likely affect customers of five utility companies indicated that electric rates would only be marginally affected. FERC's assessment of the potential impact on both large and small hydropower licensees also indicated there would be minimal impact. Further, only 1 of the 15 commenters on the proposed rulemaking raised the issue as a concern for FERC's consideration.

FERC's proposed rulemaking on changing federal land charges also includes a provision to change the annual billing cycle for administrative charges to avoid the annual $600,000 interest cost identified by DOE/IG. In our opinion, this annual interest cost reduction, coupled with the current relatively low federal land use charges, have already cost the government more than was necessary. We believe, therefore, that FERC should expedite the completion of the proposed rulemaking to the maximum extent possible consistent with sound policy practices and take appropriate steps to ensure application of the revised provisions starting January 1, 1987.

Recommendations

To ensure that all administrative costs attributable to the hydropower licensing program are recovered, we recommend that the Chairman, FERC, have the Director, Office of Program Management work with officials of the FS to apportion their administrative costs between activities under FLPMA and FPA and seek recovery of all FPA-related costs.

To ensure that FERC assesses reasonable hydropower charges for usage of federal lands and minimizes federal interest costs, we recommend that the Chairman, FERC, take steps to ensure that a final rule to revise land use charges and change the current annual administrative charge billing cycle is completed in a manner that authorizes land use charges to become effective January 1, 1987.

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